

SCOTT COUNTY HOSPITAL, INC.

FINANCIAL STATEMENTS

and

ADDITIONAL INFORMATION

with

INDEPENDENT AUDITOR'S REPORT

YEARS ENDED JUNE 30, 2017 AND 2016

George, Bowerman & Noel, P.A.

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Scott County Hospital, Inc.
Scott City, Kansas

Report on the Financial Statements

We have audited the accompanying balance sheets of Scott County Hospital, Inc. (the Hospital), a component unit of Scott County, Kansas as of June 30, 2017 and 2016, and the related statements of revenues, expenses, and changes in net position and statements of cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the provisions of the Kansas Municipal Audit and Accounting Guide. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Scott County Hospital, Inc. as of June 30, 2017 and 2016, and the changes in financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Additional Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial

statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were made for the purpose of forming opinions on the basic financial statements taken as a whole. The additional information, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the additional information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

George, Baverman & Noll, P.A.

Wichita, Kansas
January 23, 2018

SCOTT COUNTY HOSPITAL, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Scott County Hospital, Inc.'s (Hospital) management discussion and analysis presents an overview of the Hospital's financial activities for the fiscal years ended June 30, 2017 and 2016. Please read it in conjunction with the Hospital's financial statements, which begin on page 7.

Financial Highlights

- Current assets decreased by \$243,312 or 3% in 2017 and increased by \$376,852 or 4% in 2016.
- The Hospital's net patient service revenue decreased by \$1,314,056 or 7% in 2017 and by \$1,482,564 or 8% in 2016.
- Contractual allowances, bad debts and charity care reduced gross patient service revenue by \$8,262,589 or 32% of gross patient service revenue in 2017 and by \$7,153,654 or 27% of gross patient service revenue in 2016.
- The excess of operating expenses (which includes depreciation expense of \$1,977,135 and \$2,075,911) over operating revenue was \$2,291,857 and \$2,103,563 in 2017 and 2016, respectively. After including the net nonoperating revenues (taxes, interest earnings, etc.) of \$281,639 and \$342,687, the total decrease in net position was \$2,010,218 and \$1,760,876 for 2017 and 2016, respectively.

Financial Statements

The Hospital's financial statements are prepared using proprietary fund accounting that focuses on the determination of net position, changes in net position, and cash flows in a manner similar to private-sector businesses. The basic financial statements include a *balance sheet*, *statement of revenue, expenses and changes in net position*, and *statement of cash flows*, followed by notes to the financial statements and schedules of certain additional information. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The *balance sheet* presents information on the Hospital's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may indicate whether the financial position of the Hospital is improving or deteriorating.

The *statement of revenues, expenses and changes in net position* presents both the operating revenues and expenses and nonoperating revenues and expenses along with other changes in net position for the year. This statement is an indication of the success of the Hospital's operations over the past year.

The *statement of cash flows* presents the change in cash and cash equivalents for the year resulting from operating activities, noncapital financing activities, capital and related financing activities and investing activities. The primary purpose of this statement is to provide information about the Hospital's cash receipts and cash payments during the year.

Net Position

The Hospital's net position is the difference between its assets and deferred outflows of resources and its liabilities and deferred inflows of resources reported in the Balance Sheets on pages 7 and 8.

	June 30,		
	2017	2016	2015
Assets:			
Current assets	\$ 9,161,360	\$ 9,404,672	\$ 9,027,820
Capital assets, net	17,765,971	19,672,430	21,626,265
Other noncurrent assets	—	—	—
Total assets	<u>\$ 26,927,331</u>	<u>\$ 29,077,102</u>	<u>\$ 30,654,085</u>
Liabilities:			
Long-term liabilities	\$ —	\$ —	\$ —
Other liabilities	2,184,206	2,323,759	2,139,866
Total liabilities	<u>\$ 2,184,206</u>	<u>\$ 2,323,759</u>	<u>\$ 2,139,866</u>
Net position:			
Net investment in capital assets	\$ 19,743,106	\$ 19,672,430	\$ 21,626,265
Restricted	20,232	22,569	24,810
Unrestricted	4,979,787	7,058,344	6,863,144
Total net position	<u>\$ 24,743,125</u>	<u>\$ 26,753,343</u>	<u>\$ 28,514,219</u>

Recent Financial Performance

The schedule below is a summary of the Hospital's revenues, expenses and changes in net position for the past three years.

	Year ended June 30,		
	2017	2016	2015
Operating revenue	<u>\$ 18,582,103</u>	<u>\$ 19,750,904</u>	<u>\$ 17,802,364</u>
Operating expenses:			
Salaries	10,915,098	10,897,086	10,017,291
Employee benefits	2,733,061	2,650,961	2,450,720
Supplies and other	5,248,666	6,230,509	5,827,591
Depreciation and amortization	1,977,135	2,075,911	2,042,484
Total operating expenses	<u>20,873,960</u>	<u>21,854,467</u>	<u>20,338,086</u>
Operating loss	<u>(2,291,857)</u>	<u>(2,103,563)</u>	<u>(2,535,722)</u>
Nonoperating revenues:			
Taxes	186,000	222,164	331,962
Investment income	27,204	25,608	23,872
Grants and contributions – Noncapital	68,435	94,915	49,481
Total nonoperating revenues	<u>281,639</u>	<u>342,687</u>	<u>405,315</u>
Excess of expenses over revenues before capital grants and contributions	<u>(2,010,218)</u>	<u>(1,760,876)</u>	<u>(2,130,407)</u>
Grants and contributions for capital assets	<u>—</u>	<u>—</u>	<u>228,948</u>
Decrease in net position	<u>\$ (2,010,218)</u>	<u>\$ (1,760,876)</u>	<u>\$ (1,901,459)</u>
Net position at end of year	<u>\$ 24,743,125</u>	<u>\$ 26,753,343</u>	<u>\$ 28,514,219</u>

Operating Loss

The first component of the overall change in the Hospital's net position is its operating income (loss)—generally, the difference between net patient service revenue and the expenses incurred to perform those services. The Hospital reported an operating loss of \$2,291,857 and \$2,103,563 in 2017 and 2016, respectively.

The primary components of the operating loss in 2017 are:

- A decrease in net patient service revenue of \$1,314,056 or 7%. The decrease is primarily related to decreases in service levels for the routine service, pharmacy, and clinic services. Acute and swing bed patient days decreased by approximately 21%. Hospital clinic visits decreased by approximately 9%.
- Other operating revenue increased approximately \$145,000 in 2017 primarily due to increasing utilization of services under the 340B Drug Discount Program.
- Supplies and other expenses decreased by approximately \$982,000 or 16% primarily due to the decreases in the service levels in routine service, pharmacy, and clinic services noted above.

The primary components of the operating loss in 2016 are:

- An increase in net patient service revenue of \$1,482,564 or 8%. The increase is primarily related to increases in service levels for the pharmacy, imaging, and therapy services.
- Other operating revenue increased approximately \$520,000 in 2016 primarily due to the Facility qualifying for the 340B Drug Discount Program.
- Salaries and benefit expenses increased by \$879,795 and \$200,241 or 9% and 8%, respectively. These increases are due primarily to the addition of new employees to provide for the continued increase in service levels.
- Supplies and other expenses increased by \$402,918 or 7% with the increases incurred primarily in the clinic, health information, nursing, imaging, and therapy services.

The rate of healthcare inflation has a direct effect on the cost of services provided by the Hospital. A component of the Hospital's costs are expenses for medical supplies and prescription drugs. Some of the major factors contributing to the increased medical supply and drug costs include the introduction of new drugs that cannot be obtained in generic form, and changes in therapeutic mix.

Nonoperating Revenues and Expenses

The primary components of nonoperating revenues and expenses are tax revenues, investment income, and grants and contributions. The nonoperating revenues and expenses decreased approximately \$61,000 in 2017 from 2016 primarily due to a decrease in tax revenues of approximately \$36,000 and a decrease in contributions received of approximately \$26,000.

The Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in operating income and losses and nonoperating revenues and expenses, discussed earlier.

Capital Assets

The Hospital had \$17,765,971 and \$19,672,430 invested in capital assets, net of accumulated depreciation at June 30, 2017 and 2016, respectively, as detailed in Note 7 to the financial statements. The Hospital had expenditures for capital assets of \$70,676 and \$122,076 in 2017 and 2016, respectively.

Other Economic Factors

Management expects the current economic conditions to continue over the next year.

Issues Facing the Hospital

There are issues facing the Hospital that could result in material changes in its financial position in the long term. Among these issues are:

- Risks related to Medicare and Medicaid reimbursement. A significant portion of the Hospital's revenues are derived from the Medicare program, which provides certain healthcare benefits to beneficiaries who are over 65 years of age or disabled, and the Medicaid program, funded jointly by the federal government and the states, which provides medical assistance to certain needy individuals and families. The funding of these programs by the federal and state governments face increasing pressure due to the significant increases in the costs of providing healthcare services in recent years.
- Employment and labor issues. The Hospital is a major employer within the community, employing a complex mix of professional, technical, clerical, maintenance, dietary, and other workers. Risks include personal tort actions, work-related injuries and exposure to hazardous materials. A relative shortage of nursing and other medical professional/technical employees within the state, is an issue that is causing salary and benefits costs to increase at significant rates.
- Technology and services. Scientific and technological advances, new procedures, drugs and appliances, preventive medicine, and outpatient healthcare delivery may reduce utilization and revenues for the Hospital in the future. Technological advances continue to accelerate the need to acquire sophisticated and expensive equipment and services for diagnosis and treatment of illnesses and diseases.
- Increasing numbers of uninsured and underinsured patients. Due to the significant increases and high cost of healthcare insurance premiums in recent years, increasing numbers of patients of the Hospital are finding it more and more difficult to obtain or maintain adequate health insurance coverage. This trend could increase the levels of uncompensated care provided by the Hospital.

Contacting The Hospital's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hospital Administration Department, at Scott County Hospital, Inc., 301 Albert Avenue, Scott City, Kansas 67871.

SCOTT COUNTY HOSPITAL, INC.

BALANCE SHEETS

ASSETS

	June 30,	
	2017	2016
Current assets:		
Cash (Notes 1 and 3)	\$ 5,189,310	\$ 4,134,184
Assets limited as to use (Note 3)	20,232	22,569
Accounts receivable, net of allowance for doubtful accounts of \$1,033,181 in 2017 and \$1,205,529 in 2016 (Notes 1 and 4)	2,961,414	3,669,478
Employee receivables	6,789	25,681
Estimated third-party payor settlements (Note 2)	351,485	858,440
Inventories (Note 1)	491,648	531,482
Prepaid expenses and other	140,482	162,838
Total current assets	9,161,360	9,404,672
Property and equipment, at cost (Notes 1 and 7):		
Land	195,000	195,000
Land improvements	336,475	336,475
Buildings	11,313,570	11,313,570
Fixed equipment	11,402,492	11,402,492
Movable equipment	7,239,982	7,169,306
Total property and equipment	30,487,519	30,416,843
Less accumulated depreciation	12,721,548	10,744,413
Property and equipment, net of accumulated depreciation	17,765,971	19,672,430
Total assets	\$ 26,927,331	\$ 29,077,102

The accompanying notes are an integral part of the financial statements.

LIABILITIES AND NET POSITION

	June 30,	
	<u>2017</u>	<u>2016</u>
Current liabilities:		
Accounts payable	\$ 691,441	\$ 802,912
Salaries and payroll taxes payable	1,058,531	1,110,960
Compensated absences payable (Note 1)	<u>434,234</u>	<u>409,887</u>
Total current liabilities	<u>2,184,206</u>	<u>2,323,759</u>
 Total long-term liabilities	 <u>—</u>	 <u>—</u>
Total liabilities	<u>2,184,206</u>	<u>2,323,759</u>
 Net position (Notes 1 and 3):		
Net investment in capital assets	19,743,106	19,672,430
Restricted for specific operating activities	20,232	22,569
Unrestricted	<u>4,979,787</u>	<u>7,058,344</u>
Total net position	<u>24,743,125</u>	<u>26,753,343</u>
Total liabilities and net position	<u>\$ 26,927,331</u>	<u>\$ 29,077,102</u>

SCOTT COUNTY HOSPITAL, INC.

STATEMENTS OF REVENUE, EXPENSES, AND CHANGES IN NET POSITION

	Year ended June 30,	
	2017	2016
Operating revenues:		
Net patient service revenue (Note 1)	\$ 17,656,712	\$ 18,970,768
Outside services	80,311	55,476
Other	845,080	724,660
Total operating revenue	18,582,103	19,750,904
Operating expenses:		
Salaries	10,915,098	10,897,086
Employee benefits	2,733,061	2,650,961
Supplies and other	5,248,666	6,230,509
Depreciation and amortization (Note 1)	1,977,135	2,075,911
Total operating expenses	20,873,960	21,854,467
Operating loss	(2,291,857)	(2,103,563)
Nonoperating revenues:		
Tax revenues	186,000	222,164
Investment income	27,204	25,608
Noncapital grants and contributions	68,435	94,915
Total nonoperating revenues	281,639	342,687
Decrease in net position	(2,010,218)	(1,760,876)
Net position at beginning of year	26,753,343	28,514,219
Net position at end of year	\$ 24,743,125	\$ 26,753,343

The accompanying notes are an integral
part of the financial statements.

SCOTT COUNTY HOSPITAL, INC.

STATEMENTS OF CASH FLOWS

	Year ended June 30,	
	2017	2016
Cash flows from operating activities:		
Receipts from and on behalf of patients	\$ 18,871,731	\$ 19,594,389
Payments to suppliers and contractors	(5,297,947)	(6,260,480)
Payments for salaries and employee benefits	(13,676,241)	(13,414,772)
Other receipts and payments, net	<u>925,391</u>	<u>780,136</u>
Net cash flows from operating activities	<u>822,934</u>	<u>699,273</u>
Cash flows from noncapital financing activities:		
Property taxes for operations	186,000	222,164
Grants and contributions	<u>68,435</u>	<u>94,915</u>
Net cash flows from noncapital financing activities	<u>254,435</u>	<u>317,079</u>
Net cash flows from capital and related financing activities –		
Purchases of property and equipment	<u>(70,676)</u>	<u>(122,076)</u>
Cash flows from investing activities:		
Net change in employee receivables	18,892	26,583
Investment income	<u>27,204</u>	<u>25,608</u>
Net cash flows from investing activities	<u>46,096</u>	<u>52,191</u>
Increase in cash and cash equivalents	1,052,789	946,467
Cash and cash equivalents at beginning of year	<u>4,156,753</u>	<u>3,210,286</u>
Cash and cash equivalents at end of year	<u>\$ 5,209,542</u>	<u>\$ 4,156,753</u>
Reconciliation of cash and cash equivalents to balance sheets:		
Cash and cash equivalents in current assets	\$ 5,189,310	\$ 4,134,184
Cash and cash equivalents in assets limited as to use	<u>20,232</u>	<u>22,569</u>
Total cash and cash equivalents	<u>\$ 5,209,542</u>	<u>\$ 4,156,753</u>

The accompanying notes are an integral part of the financial statements.

SCOTT COUNTY HOSPITAL, INC.

STATEMENTS OF CASH FLOWS - continued

	Year ended June 30,	
	2017	2016
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	\$ (2,291,857)	\$ (2,103,563)
Adjustments to reconcile operating loss to net cash flows from operating activities:		
Depreciation and amortization	1,977,135	2,075,911
Bad debt expense	1,028,682	628,279
Net (increases) decreases in current assets:		
Accounts receivable	(320,618)	397,372
Inventories	39,834	(24,138)
Estimated third-party payor settlements	506,955	(402,030)
Other	22,356	(56,451)
Net increases (decreases) in current liabilities:		
Accounts payable	(111,471)	50,618
Salaries and payroll taxes payable	(52,429)	95,963
Compensated absences payable	24,347	37,312
Net cash flows from operating activities	<u>\$ 822,934</u>	<u>\$ 699,273</u>

SCOTT COUNTY HOSPITAL, INC.
NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies is presented to assist in understanding the Hospital's financial statements. The financial statements and notes are representations of the Hospital's management, which is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

Organization and business activity

The Hospital provides acute care, swing-bed, home health, rural health clinic, and outpatient services. The Board of County Commissioners appoints the members of the Board of Directors and a financial benefit or burden exists with Scott County. For these reasons, the Hospital is considered to be a component unit of Scott County, Kansas.

Enterprise fund accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Operating revenues and expenses

The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisitions, are reported as non-operating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and cash equivalents

For purposes of the statement of cash flows, the Hospital considers all highly liquid debt instruments with an original maturity of three months or less to be cash and cash equivalents.

Patient accounts receivable

The Hospital reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information, payer mix trends, and existing economic conditions. As a service to patients, the Hospital bills third-party payers directly and bills the patient when the patient's liability is determined. Patient accounts receivable are generally due in full when billed. If the patient is unable to pay the full amount at the time the patient is billed, the Hospital negotiates a payment plan whereby monthly payments are made by the patient on the account. Accounts are considered delinquent and subsequently written off as bad debts based on individual credit evaluation and specific circumstances of the account. If future actual default rates on accounts receivable differ from those currently anticipated, the Hospital may have to adjust its allowance for doubtful accounts, which would affect earnings in the period the adjustments are made.

Inventories

Inventories are stated at cost as determined by the first-in, first-out method.

Capital assets

The Hospital's capital assets that are \$5,000 or greater, are recorded at cost at the date of acquisition, or acquisition value at the date of donation if acquired by gift. All capital assets other than land are depreciated or amortized (in the case of capital leases) using the straight-line method of depreciation using the following estimated useful lives:

	<u>Estimated useful lives</u>
Land improvements	10 - 28 years
Buildings.....	15 - 50 years
Fixed equipment	10 - 30 years
Movable equipment	5 - 21 years

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. When depreciable property is retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is reflected as non-operating revenue (expense).

Net patient service revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, per diem payments, and discounted charges. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Charity care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy based on current poverty level guidelines. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue. The Hospital provided \$108,833 and \$52,366 of charity care for the years ended June 30, 2017 and 2016, respectively, estimated by multiplying the Hospital's cost to charge ratio by the gross uncompensated care charges associated with providing care to charity patients.

Compensated absences

Employees of the Hospital are entitled to paid time off depending on length of service and whether they are full or part time. Upon resignation, termination or retirement from service with the Hospital, employees are entitled to payment for all accrued paid time off, up to the allowable maximum. The Hospital accrues the paid time off benefits as earned.

Grants and contributions

From time to time, the Hospital receives grants and contributions from government agencies, private organizations, and individuals. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenue. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses. When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

Net position

Net position of the Hospital is classified into three components. *Net investment in capital assets* consists of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted for specific operating activities* are non-capital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital. *Unrestricted net position* is the remaining net position that does not meet the definition of *net investment in capital assets*.

Deferred inflows of resources/Deferred outflows of resources

A deferred inflow of resources is defined as an acquisition of net position applicable to a future reporting period. A deferred outflow of resources is the consumption of net position that is applicable to a future reporting period. There were no items that met the definition of a deferred outflow or a deferred inflow of resources.

Risk management

The Hospital is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; natural disasters; and employee health benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial insurance coverage in any of the three preceding years.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Hospital pays fixed premiums for annual medical malpractice coverage under an occurrence-basis policy. The Hospital accrues the expenses of its share of malpractice claim costs, if any, of reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate cost of any incident. Based on the Hospital's own claims experience, no accrual, for medical malpractice costs has been made in the accompanying financial statements.

The Hospital has implemented a partially self-funded insurance plan (Note 5) to administer its employee health insurance benefits. Liabilities under this plan are estimated based on settled claims, frequency of claims and other economic factors. Claims incurred, but not reported, are recorded as a portion of the estimated liability.

Reclassifications

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 presentation. The reclassifications had no effect on the change in net position.

Subsequent events

Subsequent events have been evaluated through January 23, 2018, which is the date the financial statements were available to be issued.

2. ESTIMATED THIRD-PARTY PAYOR SETTLEMENTS

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

- **Medicare** – Inpatient and outpatient services are paid based on cost reimbursement methodologies. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and reviews thereof by the Medicare fiscal intermediary. The Hospital's classification of patients under the Medicare program and appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital. The Hospital's Medicare cost reports have been reviewed by the Medicare fiscal intermediary through June 30, 2015.
- **Medicaid** – Effective January 1, 2013, the Hospital is reimbursed under the State of Kansas KanCare program utilizing the Medicaid fee schedule plus a cost adjustment factor.

Approximately 58% of net patient service revenue is from participation in the Medicare program for each of the years ended June 30, 2017 and 2016. Laws and regulations governing the Medicare program are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and other third-party payer programs. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and cost reimbursement.

3. CASH AND ASSETS WHOSE USE IS LIMITED

Cash and assets whose use is limited consisted of the following:

	June 30,	
	2017	2016
Unrestricted:		
Cash on hand	\$ 247	\$ 197
Demand deposit accounts	3,068,476	2,011,128
Money market accounts	1,341,903	1,391,837
Savings accounts	<u>778,684</u>	<u>731,022</u>
	<u>5,189,310</u>	<u>4,134,184</u>
Assets whose use is limited:		
Cash on hand	2,565	1,735
Money market accounts	<u>17,667</u>	<u>20,834</u>
	<u>20,232</u>	<u>22,569</u>
	<u>\$ 5,209,542</u>	<u>\$ 4,156,753</u>

Assets whose use is limited are restricted for the following purposes:

	June 30,	
	2017	2016
Emergency medical services	\$ 7,164	\$ 12,250
Indigent care	8,750	7,579
Mammography expenses	<u>4,318</u>	<u>2,740</u>
	<u>\$ 20,232</u>	<u>\$ 22,569</u>

Assets released from restrictions were as follows:

	Year ended June 30,	
	2017	2016
Emergency medical services	\$ 17,767	\$ 20,493
Indigent care	<u>9,170</u>	<u>7,530</u>
	<u>\$ 26,937</u>	<u>\$ 28,023</u>

Deposits

Custodial credit risk for deposits is the risk that in the event of bank failure, the Hospital's deposits may not be returned or the Hospital will not be able to recover collateral securities in the possession of an outside party. The Hospital's policy follows applicable State statutes and requires deposits to be 100% secured by collateral (pledged securities) valued at market, less the amount of the Federal Deposit Insurance Corporation (FDIC) insurance. State statutes define the allowable pledged securities.

At June 30, 2017, the carrying amount of the Hospital's cash and investments on deposit was \$5,206,730 with the bank balances of such accounts being \$5,315,588. Of the bank balances, \$750,000 was secured by federal depository insurance and \$4,565,588 was covered by collateral held by the Hospital's custodial banks in joint custody in the name of the Hospital and its banks. The fair value of the pledged securities held by the Hospital's custodial banks was \$5,449,388 at June 30, 2017.

The remaining carrying amount of the Hospital's cash and investments at June 30, 2017 consisted of cash on hand of \$2,812.

3. CASH AND ASSETS WHOSE USE IS LIMITED (continued)

Investment policies

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Hospital's investing activities are managed under the custody of the Hospital Chief Executive Officer. Investing is performed in accordance with investment policies adopted by the Board of Directors and in compliance with State statutes.

Applicable state statutes authorize the Hospital to invest in (1) temporary notes or no-fund warrants issued by the Hospital; (2) savings deposits, time deposits, open accounts or certificates of deposit or time certificates with maturities of not more than two years, in commercial banks, savings and loan associations and savings banks; (3) repurchase agreements with commercial banks, savings and loan associations and savings banks; (4) United States treasury bills or notes with maturities as the governing body shall determine, but not exceeding two years; and (5) the municipal investment pool maintained by the State Treasurer's office.

4. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross accounts receivable from patients and third-party payors was as follows:

	June 30,	
	2017	2016
Medicare	33%	32%
Medicaid	6	3
Blue Cross	16	20
Commercial	10	9
Self pay	35	36
	<u>100%</u>	<u>100%</u>

5. EMPLOYEE HEALTH CLAIMS

Effective October 1, 2014, a self-insured plan was instituted to provide the health, pharmacy and dental coverage of participating employees and dependents up to certain individual or family annual aggregate amounts, with commercial stop-loss insurance coverage purchased for claims in excess of the aggregate annual amount.

At each fiscal year end a provision is accrued for self-insured claims for both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors.

Activity in the Hospital's self-insured employee health claims liability during fiscal 2017 and 2016 is summarized as follows:

	Year ended June 30,	
	2017	2016
Balance, beginning of year	\$ 152,346	\$ 162,572
Current year claims incurred and changes in estimates for claims incurred in prior years:		
Employer portion	1,329,099	1,263,350
Employee portion	319,508	296,332
Claims and expenses paid	<u>(1,590,213)</u>	<u>(1,569,908)</u>
Balance, end of year	<u>\$ 210,740</u>	<u>\$ 152,346</u>

6. EMPLOYEE RETIREMENT PLAN

Prior to January 1, 2017, the Hospital maintained a 401(k) Profit Sharing Plan for the benefit of eligible employees. Under that Plan the Hospital was required to contribute three percent of eligible employees compensation for each plan year. In addition, the Plan also authorized the Hospital to make a discretionary profit sharing contribution for an amount determined at the sole discretion of the Board of Directors on an annual basis.

Effective January 1, 2017, the Hospital established the Scott County Hospital Section 457(b) Plan under Code Section 457(b) of the Internal Revenue Code ("457 Plan"). Concurrent with the establishment of the 457 Plan, the Hospital restated the 401(k) Profit Sharing Plan under the name of the Scott County Hospital Retirement Plan ("Retirement Plan"). The restated Retirement Plan removed the 401(k) features of the plan.

The total combined Hospital cost under the plans were \$544,217 and \$533,766 for 2017 and 2016, respectively.

7. CAPITAL ASSETS

Capital asset additions, disposals, and balances for the years ended June 30, 2017 and 2016 were as follows:

	Balance At June 30, 2016	Additions	Disposals	Transfers	Balance At June 30, 2017
Capital assets not being depreciated:					
Land	\$ 195,000	\$ —	\$ —	\$ —	\$ 195,000
Total capital assets not being depreciated	195,000	—	—	—	195,000
Capital assets being depreciated:					
Land improvements	336,475	—	—	—	336,475
Buildings	11,313,570	—	—	—	11,313,570
Fixed equipment	11,402,492	—	—	—	11,402,492
Movable equipment	7,169,306	70,676	—	—	7,239,982
Total capital assets being depreciated	30,221,843	70,676	—	—	30,292,519

7. CAPITAL ASSETS (continued)

	Balance At June 30, 2016	Additions	Disposals	Transfers	Balance At June 30, 2017
Less accumulated depreciation for:					
Land improvements	\$ 154,972	\$ 31,389	\$ —	\$ —	\$ 186,361
Buildings	2,494,916	541,678	—	—	3,036,594
Fixed equipment	3,145,444	730,018	—	—	3,875,462
Movable equipment	4,949,081	674,050	—	—	5,623,131
Total accumulated depreciation	10,744,413	1,977,135	—	—	12,721,548
Total capital assets being depreciated, net	19,477,430	(1,906,459)	—	—	17,570,971
Total capital assets, net	<u>\$ 19,672,430</u>	<u>\$ (1,906,459)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 17,765,971</u>
	Balance At June 30, 2015	Additions	Disposals	Transfers	Balance At June 30, 2016
Capital assets not being depreciated:					
Land	\$ 195,000	\$ —	\$ —	\$ —	\$ 195,000
Total capital assets not being depreciated	195,000	—	—	—	195,000
Capital assets being depreciated:					
Land improvements	336,475	—	—	—	336,475
Buildings	11,302,070	11,500	—	—	11,313,570
Fixed equipment	11,402,492	—	—	—	11,402,492
Movable equipment	7,058,730	110,576	—	—	7,169,306
Total capital assets being depreciated	30,099,767	122,076	—	—	30,221,843
Less accumulated depreciation for:					
Land improvements	123,496	31,476	—	—	154,972
Buildings	1,933,994	560,922	—	—	2,494,916
Fixed equipment	2,412,686	732,758	—	—	3,145,444
Movable equipment	4,198,326	750,755	—	—	4,949,081
Total accumulated depreciation	8,668,502	2,075,911	—	—	10,744,413
Total capital assets being depreciated, net	21,431,265	(1,953,835)	—	—	19,477,430
Total capital assets, net	<u>\$ 21,626,265</u>	<u>\$ (1,953,835)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 19,672,430</u>

8. OTHER POST EMPLOYMENT BENEFITS

As provided by K.S.A. 12-5040, the Hospital is required to allow qualifying retirees to participate in the group health insurance plan. While each retiree is required to pay the full amount of the applicable premium, conceptually, the Hospital is subsidizing the retirees because each participant is charged a level premium regardless of age. However, the cost of the subsidy, if any, has not been quantified in these financial statements and management believes any impact on the financial statements is not significant.

Under the Consolidated Omnibus Budget Reconciliation Act (COBRA), the Hospital makes health care benefits available to eligible former employees and their eligible dependents. Certain requirements are outlined by the federal government for this coverage. The premium is paid entirely by the insured and there is no cost to the Hospital under this plan.

ADDITIONAL INFORMATION

SCOTT COUNTY HOSPITAL, INC.
Patient Service Revenue

	Year Ended June 30, 2017					Year Ended June 30, 2016				
	Inpatient	Swing Bed	Outpatient	Total	% of Patient Service Revenue	Inpatient	Swing Bed	Outpatient	Total	% of Patient Service Revenue
Routine service	\$ 978,932	\$ 1,070,029	\$ 379,562	\$ 2,428,523	9.38%	\$ 1,346,887	\$ 1,175,323	\$ 241,635	\$ 2,763,845	10.55%
Nursery	73,766	—	—	73,766	0.28%	80,074	—	—	80,074	0.31%
Operating room	134,394	17,215	1,127,423	1,279,032	4.93%	261,279	14,249	860,344	1,135,872	4.35%
Delivery room	38,404	—	—	38,404	0.15%	41,779	—	—	41,779	0.16%
Anesthesiology	75,953	12,225	584,706	672,884	2.60%	87,973	11,713	558,211	657,897	2.52%
Radiology	33,627	16,209	632,329	682,165	2.63%	60,430	23,477	617,587	701,494	2.69%
MRI	22,405	9,280	610,662	642,347	2.48%	45,210	2,602	588,680	636,492	2.44%
CT scan	126,530	26,420	1,770,456	1,923,406	7.42%	210,085	32,809	1,442,352	1,685,246	6.45%
Nuclear medicine	6,272	1,119	199,615	207,006	0.80%	3,284	2,219	261,538	267,041	1.02%
Ultrasound	57,193	9,059	678,390	744,642	2.87%	78,531	29,737	714,047	822,315	3.15%
Sleep study	306	—	171,452	171,758	0.66%	—	—	208,600	208,600	0.80%
Laboratory	358,315	181,396	3,446,037	3,985,748	15.38%	487,361	196,605	3,114,629	3,798,595	14.54%
Respiratory therapy	277,190	385,474	170,779	833,443	3.22%	418,735	463,471	138,518	1,020,724	3.91%
Physical therapy	49,892	242,961	1,187,246	1,480,099	5.71%	42,222	222,540	1,272,810	1,537,572	5.89%
Occupational therapy	51,912	191,373	254,683	497,968	1.92%	33,858	185,398	168,159	387,415	1.48%
Speech therapy	—	707	10,916	11,623	0.04%	—	—	—	0	0.00%
Electrocardiology	15,606	4,800	240,285	260,691	1.01%	20,270	6,232	230,591	257,093	0.98%
Medical supplies	49,848	29,441	134,949	214,238	0.83%	65,597	63,695	156,908	286,200	1.10%
Pharmacy	462,642	591,825	2,370,060	3,424,527	13.21%	713,215	646,160	1,993,951	3,353,326	12.84%
Treatment room	8,414	6,731	1,320,016	1,335,161	5.15%	8,338	7,998	1,083,164	1,099,500	4.21%
Emergency room	40,542	798	1,085,466	1,126,806	4.35%	67,544	—	966,214	1,033,758	3.96%
Clinic	616	—	3,157,526	3,158,142	12.18%	1,022	—	3,618,874	3,619,896	13.86%
Cardiac rehabilitation	—	—	238,560	238,560	0.92%	—	—	165,252	165,252	0.63%
Durable medical equipment	—	—	262,920	262,920	1.01%	—	—	286,977	286,977	1.10%
Ambulance	8,487	14,991	201,964	225,442	0.87%	38,367	19,312	219,780	277,459	1.06%
Total ancillary services	<u>\$ 2,871,246</u>	<u>\$ 2,812,053</u>	<u>\$ 20,236,002</u>	25,919,301	100.00%	<u>\$ 4,112,061</u>	<u>\$ 3,103,540</u>	<u>\$ 18,908,821</u>	26,124,422	100.00%
Contractual adjustments				(7,098,768)	(27.39%)				(6,462,778)	(24.74%)
Charity care				(135,139)	(0.52%)				(62,597)	(0.24%)
Bad debts				(1,028,682)	(3.97%)				(628,279)	(2.40%)
Net patient service revenue				<u>\$ 17,656,712</u>	<u>68.12%</u>				<u>\$ 18,970,768</u>	<u>72.62%</u>

SCOTT COUNTY HOSPITAL, INC.
Operating Expenses By Functional Division

	Year Ended June 30, 2017						Year Ended June 30, 2016					
	Salaries	Employee Benefits	Supplies and Other	Depreciation	Total	% of Total Operating Expenses	Salaries	Employee Benefits	Supplies and Other	Depreciation	Total	% of Total Operating Expenses
Routine services:												
Acute and swing bed	\$ 1,584,108	\$ 349,643	\$ 265,806	\$ 81,819	\$ 2,281,376	10.92%	\$ 1,534,811	\$ 387,956	\$ 423,082	\$ 84,211	\$ 2,430,060	11.14%
Nursery	2,029	2,640	2,552	272	7,493	0.04%	5,361	1,020	2,828	273	9,482	0.04%
Total routine services	1,586,137	352,283	268,358	82,091	2,288,869	10.96%	1,540,172	388,976	425,910	84,484	2,439,542	11.18%
Ancillary services:												
Operating room	300,151	91,283	199,576	71,961	662,971	3.18%	342,103	93,519	279,481	66,741	781,844	3.58%
Delivery room	14,027	18,193	25,094	6,303	63,617	0.30%	21,640	3,838	17,949	6,320	49,747	0.23%
Anesthesia	501,052	106,368	62,100	19,501	689,021	3.30%	481,801	106,834	68,028	24,764	681,427	3.12%
Radiology	223,932	47,636	42,902	47,443	361,913	1.73%	211,707	44,373	56,944	63,065	376,089	1.72%
MRI	27,347	6,465	102,357	84,670	220,839	1.06%	26,159	6,331	52,612	84,902	170,004	0.78%
CT scan	74,022	10,874	83,399	–	168,295	0.81%	67,036	10,501	81,682	–	159,219	0.73%
Sleep study	51,984	15,254	10,153	12,499	89,890	0.43%	56,456	15,313	46,437	12,533	130,739	0.60%
Nuclear medicine	27,949	4,706	119,855	–	152,510	0.73%	27,778	4,949	98,967	–	131,694	0.60%
Ultrasound	66,408	17,179	15,798	20,331	119,716	0.57%	64,277	16,500	17,205	20,387	118,369	0.54%
Laboratory	391,993	112,973	529,723	49,020	1,083,709	5.19%	392,120	106,828	535,992	56,664	1,091,604	4.99%
Blood administration	–	–	35,547	–	35,547	0.17%	–	–	48,864	–	48,864	0.22%
Respiratory therapy	253,847	59,195	12,499	4,737	330,278	1.58%	225,596	48,532	104,081	4,750	382,959	1.75%
Physical therapy	447,896	122,194	12,214	2,100	584,404	2.80%	402,884	106,834	19,722	682	530,122	2.43%
Occupational therapy	155,104	34,770	16,886	–	206,760	0.99%	125,295	20,230	31,552	–	177,077	0.81%
Speech therapy	–	–	8,390	–	8,390	0.04%	–	–	–	–	–	– %
Electrocardiology	7,715	1,684	427	1,790	11,616	0.06%	9,647	2,103	128	3,084	14,962	0.07%
Medical supplies	87,004	20,611	7,210	1,307	116,132	0.56%	80,778	23,410	24,711	1,311	130,210	0.60%
Pharmacy	128,430	19,334	1,022,067	6,872	1,176,703	5.64%	117,016	15,723	1,269,922	8,211	1,410,872	6.46%
Treatment room	329,934	77,091	177,485	527	585,037	2.80%	310,069	73,027	122,146	529	505,771	2.31%
Emergency room	370,901	77,530	85,894	6,285	540,610	2.59%	378,964	85,401	105,519	6,383	576,267	2.64%
Clinic	3,075,097	650,919	323,738	4,802	4,054,556	19.42%	3,156,491	631,195	643,767	53,826	4,485,279	20.52%
Cardiac rehabilitation	78,515	10,138	4,217	8,933	101,803	0.49%	62,242	7,571	2,777	8,957	81,547	0.37%
Durable medical equipment	106,922	21,643	121,060	292	249,917	1.20%	95,043	19,301	134,829	878	250,051	1.14%
Ambulance	128,223	48,605	45,937	138	222,903	1.07%	125,797	38,375	56,985	253	221,410	1.01%
Total ancillary services	6,848,453	1,574,645	3,064,528	349,511	11,837,137	56.71%	6,780,899	1,480,688	3,820,300	424,240	12,506,127	57.22%
General services:												
Nursing administration	190,119	48,276	1,925	–	240,320	1.15%	182,539	39,563	1,058	–	223,160	1.02%
Operation of plant	118,515	35,470	623,269	2,301	779,555	3.73%	122,382	37,673	633,671	2,307	796,033	3.64%
Laundry	59,258	23,900	12,489	1,975	97,622	0.47%	55,145	21,296	12,489	1,980	90,910	0.42%
Housekeeping	178,892	55,740	39,975	–	274,607	1.32%	177,391	49,780	39,212	–	266,383	1.22%
Nutritional services	220,511	68,636	225,546	2,539	517,232	2.48%	216,527	74,460	233,645	2,835	527,467	2.41%
Health information	482,550	151,603	253,199	200,102	1,087,454	5.21%	431,991	132,807	202,577	196,946	964,321	4.41%
Administration and general	1,064,406	304,978	678,179	35,364	2,082,927	9.98%	1,222,053	297,702	779,719	37,801	2,337,275	10.69%
Employee benefits	166,257	117,530	81,198	163	365,148	1.75%	167,987	128,016	81,928	164	378,095	1.73%
equipment/buildings	–	–	–	1,303,089	1,303,089	6.24%	–	–	–	1,325,154	1,325,154	6.06%
Total general services	2,480,508	806,133	1,915,780	1,545,533	6,747,954	32.33%	2,576,015	781,297	1,984,299	1,567,187	6,908,798	31.60%
Total expenses	\$10,915,098	\$ 2,733,061	\$ 5,248,666	\$ 1,977,135	\$20,873,960	100.00%	\$10,897,086	\$ 2,650,961	\$ 6,230,509	\$ 2,075,911	\$21,854,467	100.00%